

Internal Revenue Service
Appeals Office
1375 E. Ninth Street, Suite 815
Cleveland, OH 44114-1739

Department of the Treasury

Person to Contact:

Number: **201140031**
Release Date: 10/7/2011

Refer Reply to:

Date: July 15, 2011

In Re:
EO Revocation
Tax Period(s) Ended:

A

Form Required to be Filed:

B

Employer Identification Number:
D
UIL:
501.03-00

Certified Mail

Dear :

This is a final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code (IRC). It is determined that you do not qualify as exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code, effective January 1, 2007.

Our adverse determination was made for the following reason(s):

A substantial part of your activities consists of providing down payment assistance to home buyers. To finance the assistance you rely on home sellers and other real-estate related businesses that stand to benefit from these down payment assistance transactions. Your receipt of a payment from the home seller corresponds to the amount of the down payment assistance provided in substantially all of your down payment assistance transactions. The manner in which you operate demonstrates that you are not operated to further the interests of a charitable class. Therefore, you are operated for a substantial nonexempt purpose. In addition, your operations further the private interests of the persons that finance your activities. Accordingly, you are not operated exclusively for exempt purposes described in section 501(c)(3).

Contributions to your organization are not deductible under Code section 170.

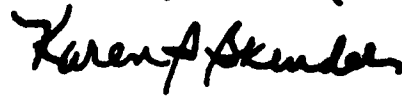
You are required to file Federal income tax returns on the form indicated above. You should file these returns within 30 days from the date of this letter, unless a request for

an extension of time is granted. File the returns in accordance with their instructions, and do not send them to this office. Processing of income tax returns and assessment of any taxes due will not be delayed because you have filed a petition for declaratory judgment under Code section 7428.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, a petition to the United States Tax Court, the United States Court of Federal Claims, or the district court of the United States for the District of Columbia must be filed within 90 days from the date this determination was mailed to you. Contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

A handwritten signature in black ink, appearing to read "Karen A. Skinder". The signature is fluid and cursive, with the first name "Karen" being more prominent.

Karen A. Skinder
Appeals Team Manager



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
Internal Revenue Service
1100 Commerce Street, MC4915:DAL
Dallas, Texas 75242

March 11, 2010

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

Letter 3618 (04-2002)
Catalog Number 34809F

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Acting Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
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ISSUE

Whether ORG (ORG) operated exclusively for exempt purposes within the meaning of I.R.C. § 501(c)(3)?

FACTS

Overview

ORG was incorporated in State on January 14, 20XX as a for-profit entity. On July 14, 20XX, ORG amended its articles of incorporation to change its status to that of a nonprofit corporation. NAME is the registered agent and president. The organization's address is XXXXXXXXXX.

ORG filed Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, on March 18, 20XX. By letter dated August 29, 20XX, based on the information ORG provided in its application for exemption (and subsequent related correspondence) and on the assumption that ORG would operate in the manner represented in its application (and additional information provided), the Internal Revenue Service (IRS) recognized ORG, as a tax exempt organization as described in section 501(c)(3) as of January 14, 20XX.

ORG has promoted and operated a down payment assistance (DPA) program for home buyers from 20XX through October of 20XX. Through its DPA program, ORG provided funds to home buyers to use as the down payments or for closing costs and in turn collected the same amount, plus an additional fee, from the house sellers. As more fully described below, under ORG program, down payment assistance was provided for FHA housing loan programs without any income or asset limitations.

Application for Recognition of Tax Exempt Status

As discussed above, on March 18, 20XX, ORG filed an application for exemption with the IRS. In that application ORG stated the following as its purpose:

The purpose of the organization is to provide individuals and families who desire to purchase a home, but are without the financial resource, to raise the required down payment, with the financial support in the form of a grant from this non-profit organization we are forming to allow the dream of being a homeowner to become possible.

During the consideration of the application, the IRS requested that ORG clarify its proposed activity with respect to income limits and financial need. ORG stated in its

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reply letter to Internal Revenue Service on May 20, 20XX, "The class of potential recipients of grants will be home buyers that are low to moderate income families and individuals with a steady job. There will be no specific restrictions on who may apply or whom will be considered as possible grantees other than those individuals or families who would not otherwise be approved for mortgage loan in order to make monthly payments on the mortgage loan."

By letter dated June 4, 20XX, the IRS advised ORG, "Since you do not limit your assistance to a charitable class of individuals such as low-income individuals it does not appear that your program qualifies for exemption under section 501(c)(3) of the Code."

ORG stated in an attachment to a letter to the IRS dated July 10, 20XX that it had amended Article 3 of its Articles of Incorporation to include the following:

ORG will only provide down payment assistance to individuals that qualify as low-income. Low income families will be identified in accordance with the income limits computed and published by the Department of Housing and Urban Development [HUD] in Income Limits for Low and Very Low-Income Families under the Housing act of 1937. The term "low-income" is defined by the statute as 80 percent of the area's median income.

Concerning financial support, ORG stated in its application, , "The source of financial support will be in the form of donations from churches, businesses, individuals, banks, mortgage companies and community re-investment programs."

Federal Returns

ORG filed Form 990 for the calendar year ended December 31, 20XX. In 20XX, the only reported activity was the operation of its DPA program, described in more detail below.

According to Part III of the 2007 Form 990, the primary exempt purpose of ORG was "to assist families [to] purchase homes." It stated the following as its accomplishment during 20XX: "Provide down payment assistance to help low to moderate income families purchase homes.

In 20XX and 20XX, ORG reported revenue in the amounts of \$ and \$ respectively. Of those amounts \$ (all) and \$ (most) were paid to ORG by sellers participating in the ORG DPA program in 20XX

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and 20XX, respectively. ORG characterized these payments as program service revenue.

ORG reported that it distributed \$ in 20XX and \$ in 20XX in down payment assistance to homebuyers for use as down payments and/or to pay for closing costs. The balance of its expenditures was reported as paid for the categories "Management and general" and "Fundraising."

DPA Program.

ORG promoted its DPA program to builders, lenders, loan officers, mortgage brokers, real estate agents, buyers, and sellers through its website (WEBSITE), flyers, advertising, and other methods,

Most, if not all, of the participants in the ORG DPA program utilized Federal Housing Administration (FHA) financing for their home purchase.

The ORG website described the down payment assistance program as follows:

1. Buyer qualifies for a loan from a lender that accepts Non-Profit gift donations.
2. Seller agrees to utilize the program and then signs one required form called the Seller's Agreement .
3. The Lender completes a one-page online gift request form and has the Buyer sign the gift letter.
4. The gift funds are then wired to the closing attorney/agent the day before the closing date.
5. The Seller pays a service fee to American Homebuyers after the closing to replenish the pool of funds for future gifts.

Through the ORG DPA program, buyers receive a "gift/grant" of the funds they use for the down payment. During the years under examination, the down payment "gift/grants" were amounts as determined by the lender; often the amount was 3% of the property's stated sales price.

A home buyer was eligible to participate in the ORG DPA program only if the buyer purchased a house from a seller who agreed to ORG contractual terms. ORG and the sellers entered into agreements requiring sellers to pay ORG an amount equal to the

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down payment "gift/grant" that the buyer received under the ORG DPA program and an additional "processing fee," usually an amount between \$295.00 and \$450.00.

Although ORG stated that the seller's payment was not provided directly to the buyer, but instead was used to "replenish" the pool of funds used to provide "gift/grants" to subsequent buyers, in essence, these transactions resulted in a circular flow of the money. The sellers made payments to ORG. ORG provided the funds to the buyers; the buyers used the funds to make the down payment necessary to purchase a home from the sellers, thereby returning the funds to the sellers.

Despite the representations in its amended articles of incorporation provided during the application for exemption process, ORG did not have any income limitations for its DPA program and did not screen applicants for down payment assistance based on income. The records provided by ORG did not include data on the buyers' incomes and gave no indication that ORG screened for this data.

Rather, the ORG DPA program provided "gifts" to any homebuyers who qualified for loans. ORG promotional material and advertising made it clear anyone who could qualify for some type of loan was eligible for the ORG DPA.

In addition, ORG documents (from their website) explicitly state the down payment "gift/grant" to a buyer comes from preexisting ORG funds rather than from the seller's payment in the transaction. ORG does not solicit outside public contributions nor does it have any source of funds other than payments from sellers. Since the seller of a property is required to make a payment to ORG equal to the amount of the down payment assistance provided to the buyer, plus the fee to ORG, the actual source of the down payment assistance is, in effect, the seller's "gift/grant."

In 20 , ORG brokered DPA to over 1,000 home buyers.

ORG did not promote its DPA program by advising house sellers and others that sellers may claim charitable deductions on their federal income tax returns for amounts they pay to ORG. On its website, (WEBISTE) its advertisements, and in other promotional materials, ORG states that its "fee is not tax deductible as a charitable contribution because the seller derives the full benefit of the contribution through the sale of a home. "

Each seller's contract obligates the seller, in consideration for participating in the ORG program, to pay ORG an amount equal to the amount of the DPA received by the buyer and an additional processing fee. The contract, which was required to be signed by each participating seller, stated, "If for any reason this property does not close or the property closes without using the ORG Gift Funds, the seller is under no obligation to pay this service fee."

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The parties to the down payment assisted real estate transactions, including the sellers, realtors, builders and lenders, benefited more than incidentally from ORG operations. The following information, taken from some of ORG promotional materials, clearly demonstrates this benefit.

Lenders

ORG promotional materials told lenders that using ORG DPA program will provide the following benefits:

- Save thousands of dollars by eliminating potential fines and/or buy backs at no direct cost!
- Avoid the HUD Neighborhood Watch and Credit Watch Termination List!
- Stay ahead of the Competition by improving pricing from the investors!
- Gain access to a vehicle that would potentially make mortgage payments on behalf of the homebuyer!
- Effectively eliminate delinquencies, defaults, and foreclosures.

ORG provided DPA not only to home buyers in the STATE, STATE area, it also provided assistance to home buyers in several other states including, SATE, STATE, and STATE.

ORG1.

The President of ORG, NAME, is the sole owner of ORG1 (ORG1), a for-profit entity incorporated in State. Although ORG1 had limited activity; all of its income was from transactions associated with ORG. In the year 20XX, it received \$ under this program.

Other Activities

NAME, President of ORG, reported in interviews on October 7th and 8th of 20XX that ORG has also made house payments on a case-by-case basis for its DPA clients with financial difficulties. He reported that it made house payments in the amount of \$(in 20 In comments concerning the interview notes, NAME added that ORG assisted many homeowners in loss mitigation by preparing workout packages with the servicing lenders. He also stated that ORG educated hundreds of borrowers with their Homebuyers Education Courses.

stated further that ORG has not operated a DPA program since October of 20XX

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and that the focus of ORG since that time has been on homebuyer education and foreclosure prevention. Details as to numbers of people served and amounts expended in those activities were not provided.

LAW

Section 501 of the Code provides for the exemption from federal income tax of corporations organized and operated exclusively for charitable or educational purposes, provided that no part of the net earnings of such corporations inures to the benefit of any private shareholder or individual. See IRC § 501(c)(3).

Treasury Regulation section 1.501(c)(3)-1(c)(1) provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in section 501(c)(3). An organization must not engage in substantial activities that fail to further an exempt purpose. In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279, 283 (1945), the Supreme Court held that the "presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

Treasury Regulation section 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. To meet this requirement, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests.

Treasury Regulation section 1.501(c)(3)-1(d)(2) defines the term "charitable" for section 501(c)(3) purposes as including the relief of the poor and distressed or of the underprivileged, and the promotion of social welfare by organizations designed to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration. The term "charitable" also includes the advancement of education. Id.

Treasury Regulation section 1.501(c)(3)-1(d)(3)(i) provides, in part, that the term "educational" for section 501(c)(3) purposes relates to the instruction of the public on subjects useful to the individual and beneficial to the community.

Treasury Regulation section 1.501(c)(3)-1(e) provides that an organization that operates a trade or business as a substantial part of its activities may meet the requirements of section 501(c)(3) if the trade or business furthers an exempt purpose, and if the organization's primary purpose does not consist of carrying on an unrelated trade or business.

In Easter House v. United States, 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir. 1988), the U.S. Court of Federal Claims considered whether an organization that

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provided prenatal care and other health-related services to pregnant women, including delivery room assistance, and placed children with adoptive parents qualified for exemption under section 501(c)(3). The court concluded that the organization did not qualify for exemption under section 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization's argument that the adoption services merely complemented the health-related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization's operation of an adoption service, which, in and of itself, did not serve an exempt purpose.

The organization's sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. In addition, although the organization provided health care to indigent pregnant women, it only did so when a family willing to adopt a woman's child sponsored the care financially. Accordingly, the court found that the "business purpose, and not the advancement of educational and charitable activities purpose, of plaintiff's adoption service is its primary goal" and held that the organization was not operated exclusively for purposes described in section 501(c)(3). Easter House, 12 Cl. Ct. at 485-486.

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the court held that an organization that operated a school to train individuals for careers as political campaign professionals, but that could not establish that it operated on a nonpartisan basis, did not exclusively serve purposes described in section 501(c)(3) because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with entities of a particular political party and that most of the organization's graduates worked in campaigns for the party's candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting the party's candidates and entities. Although the candidates and entities benefited were not organization "insiders," the court stated that the conferral of benefits on disinterested persons who are not members of a charitable class may cause an organization to serve a private interest within the meaning of Treasury Regulation section 1.501(c)(3)-1(d)(1)(ii). The court concluded by stating that even if the political party's candidates and entities did "comprise a charitable class, [the organization] would bear the burden of proving that its activities benefited members of the class in a non-select manner." American Campaign Academy, 92 T.C. at 1077.

In Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), the court held that an organization that marketed handicrafts made by disadvantaged artisans through museums and other non-profit organizations and shops operated for exclusively

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charitable purposes within the meaning of section 501(c)(3). The organization, in cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in communities identified as disadvantaged based on objective evidence collected by the Bureau of Indian Affairs or other government agencies. The organization marketed only handicrafts it purchased in bulk from communities of craftsmen. The organization did not market the kind of products produced by studio craftsmen, nor did it market the handicrafts of artisans who were not disadvantaged. The court concluded that the overall purpose of the organization's activity was to benefit disadvantaged communities. The organization's commercial activity was not an end in itself but the means through which the organization pursued its charitable goals. The method the organization used to achieve its purpose did not cause it to serve primarily private interests because the disadvantaged artisans directly benefited by the activity constituted a charitable class and the organization showed no selectivity with regard to benefiting specific artisans. Therefore, the court held that the organization operated exclusively for exempt purposes described in section 501(c)(3).

In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the court relied on the commerciality doctrine in applying the operational test. Because of the commercial manner in which the organization conducted its activities, the court found that it was operated for a nonexempt commercial purpose, rather than for a tax exempt purpose. As the court stated:

Among the major factors courts have considered in assessing commerciality are competition with for-profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, inter alia, whether the organization uses commercial promotional methods (e.g. advertising) and the extent to which the organization receives charitable donations.

See also, Living Faith Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991) (holding that a religious organization which ran restaurants and health food stores in furtherance of its health ministry did not qualify for tax exempt status because it was operated for substantial commercial purposes and not for exclusively exempt purposes).

Revenue Ruling 67-138, 1967-1 C.B. 129, held that helping low-income persons obtain adequate and affordable housing is "charitable" because it relieves the poor and distressed or underprivileged. In Revenue Ruling 67-138, the organization carried on several activities directed to assisting low-income families in obtaining improved housing, including (1) conducting a training course relative to various aspects of homebuilding and homeownership, (2) coordinating and supervising joint construction projects, (3) purchasing building sites for resale at cost, and (4) lending aid in obtaining home construction loans.

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Revenue Ruling 70-585, 1970-2 C.B. 115, discussed four situations of organizations providing housing and analyzed whether each organization qualified as charitable within the meaning of section 501(c)(3). Situation 1 described an organization formed to construct new homes and renovate existing homes for sale to low-income families who could not obtain financing through conventional channels. The organization also provided financial aid to low-income families eligible for loans, under a Federal housing program, which did not have the necessary down payment. The organization made rehabilitated homes available to families who could not qualify for any type of mortgage. When possible, the organization recovered the cost of the homes through very small periodic payments, but its operating funds were obtained from federal loans and contributions from the general public. The revenue ruling held that by providing homes for low-income families who otherwise could not afford them, the organization relieved the poor and distressed.

Situation 2 described an organization formed to improve the housing needs of minority groups by building housing units for sale to persons of low and moderate-income on an open-occupancy basis. The housing was made available to members of minority groups who were unable to obtain adequate housing because of local discrimination. The housing units were located to help reduce racial and ethnic imbalances in the community. As the activities were designed to eliminate prejudice and discrimination and to lessen neighborhood tensions, the revenue ruling held that the organization was engaged in charitable activities within the meaning of section 501(c)(3).

Situation 3 described an organization formed to formulate plans for the renewal and rehabilitation of a particular area in a city as a residential community. The median income level in the area was lower than in other sections of the city and the housing in the area generally was old and badly deteriorated. The organization developed an overall plan for the rehabilitation of the area, sponsored a renewal project, and involved residents in the area renewal plan. The organization also purchased an apartment building that it rehabilitated and rented at cost to low and moderate-income families with a preference given to residents of the area. The revenue ruling held that the organization was described in section 501(c)(3) because its purposes and activities combated community deterioration.

Situation 4 described an organization formed to alleviate a shortage of housing for moderate-income families in a particular community. The organization planned to build housing to be rented at cost to moderate-income families. The Service held that the organization failed to qualify for exemption under section 501(c)(3) because the organization's program was not designed to provide relief to the poor or further any other charitable purpose within the meaning of section 501(c)(3) and the regulations.

In early 2006 the IRS issued Revenue Ruling 2006-27, 2006-1 C.B. 915, which describes three organizations involved in providing down payment assistance and

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determines whether each qualifies for exempt status under section 501(c)(3). The organization described in Situation 1 makes assistance available to low-income families to purchase decent and safe homes throughout the metropolitan area in which it is located. Individuals are eligible to participate if they are low-income and have the employment history and financial history to qualify for a mortgage with the exception that they do not have the funds necessary for down payments.

The organization in Situation 1 offers financial seminars, conducts educational activities to prepare the individuals for home ownership, and requires a home inspection report before providing funds for down payment assistance. To fund the program, the organization conducts broad based fundraising that attracts gifts, grants, and contributions from the general public. Further, the organization has policies in place to ensure that the grant making staff does not know the identity or contributor status of the home seller or other parties who may benefit from the sale and does not accept contributions contingent on the sale of particular properties.

Because the organization described in Situation 1 relieves the poor and distressed, requires a home inspection to insure that the house is habitable, conducts educational seminars, has a broad based funding program, and has policies to ensure that the organization is not beholden to particular donors, the Service held that the organization is operated exclusively for charitable purposes and qualifies for exemption from federal taxation as an organization described in section 501(c)(3).

The organization described in Situation 2 of Revenue Ruling 2006-27, is like that described in Situation 1, except that (1) its staff knows the identity of the party selling the home and may know the identity of other parties involved in the sale; (2) the organization receives a payment from the seller (the amount of which bears a direct correlation to the amount of down payment assistance provided) in substantially all the cases in which the organization provides assistance to the home buyers; and (3) most of its financial support comes from home sellers and related businesses that may benefit from the sale of homes to buyers who receive assistance from the organization.

Because, the organization described in Situation 2 provides down payment assistance amounts that directly correlate to the amounts provided by home sellers and relies primarily on payments from home sellers and real-estate related businesses that stand to benefit from the transactions to finance its program, the Service held that the organization described in Situation 2 is not operated exclusively for exempt purposes and does not qualify for exemption from federal income tax as an organization described in section 501(c)(3).

Situation 3, describes an organization that is restricting its activities to a particular area in a city as a residential community. ORG not only did not confine itself to a community in the STATE area, but provided loans through the STATE and to other STATES as

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previously mentioned. There is no indication that the organization limited its loans to blighted areas.

Benefiting Private Interests

Even if an organization's activities serve a charitable class or are otherwise charitable within the meaning of section 501(c)(3), it must demonstrate that its activities serve a public rather than a private interest within the meaning of Treasury Regulation section 1.501(c)(3)-1(d)(1).

Revenue Ruling 72-147, 1972-1 C.B. 147, held that an organization that provided housing to low income families did not qualify for exemption under section 501(c)(3) because it gave preference to employees of business operated by the individual who also controlled the organization. The ruling reasoned that, although providing housing for low-income families furthers charitable purposes, doing so in a manner that gives preference to employees of the founder's business primarily serves the private interest of the founder rather than a public interest.

In KJ's Fund Raisers v. Commissioner, T.C. Memo 1997-424 (1997), *aff'd*, 166 F.3d 1200 (2d Cir. 1998), the Tax Court held, and the Second Circuit affirmed, that an organization formed to raise funds for distribution to charitable causes did not qualify for exemption under section 501(c)(3) because its activities resulted in a substantial private benefit to its founders. The founders of the organization were the sole owners of KJ's Place, a lounge at which alcoholic beverages were served. The founders served as officers of the organization and, at times, also controlled the organization's board. The Tax Court found, and the Second Circuit agreed, that the founders exercised substantial influence over the affairs of the organization. The organization's business consisted of selling "Lucky 7" or similar instant win lottery tickets to patrons of KJ's Place. The organization derived most of its funds from its lottery ticket sales. The organization solicited no public donations. The lottery tickets were sold during regular business hours by the owners of the lounge and their employees. From the proceeds of the sales of the lottery tickets, the organization made grants to a variety of charitable organizations. Although supporting charitable organizations may be a charitable activity, the Tax Court nevertheless upheld the Commissioner's denial of exemption to the organization on the ground that the organization's operation resulted in more than incidental private benefit. The Tax Court held, and the Second Circuit affirmed, that a substantial purpose of KJ's activities was to benefit KJ's place and its owners by attracting new patrons, by way of lottery ticket sales, to KJ's Place, and by discouraging existing customers from abandoning KJ's Place in favor of other lounges where such tickets were available. Thus, the organization was not operated exclusively for exempt purposes within the meaning of section 501(c)(3).

Effective date of revocation

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An organization may ordinarily rely on a favorable determination letter received from the Internal Revenue Service. Treas. Reg. §1.501(a)-1(a)(2); Rev. Proc. 2003-4, §14.01 (cross-referencing §13.01 et seq.), 2003-1 C.B. 123. An organization may not rely on a favorable determination letter, however, if the organization omitted or misstated a material fact in its application or in supporting documents. In addition, an organization may not rely on a favorable determination if there is a material change, inconsistent with exemption, in the organization's character, purposes, or methods of operation after the determination letter is issued. Treas. Reg. § 601.201(n)(3)(ii); Rev. Proc. 90-27, 1990-1 C.B. 514, §13.02.

The Commissioner may revoke a favorable determination letter for good cause. Treas. Reg. § 1.501(a)-1(a)(2). Revocation of a determination letter may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. Treas. Reg. § 601.201(n)(6)(i), § 14.01; Rev. Proc. 2003-4, § 14.01 (cross-referencing § 13.01 et seq.).

GOVERNMENT'S POSITION

ORG does not operate exclusively for exempt purposes as an organization described in section 501(c)(3) because it operates a program that does not exclusively serve an exempt purpose described in section 501(c)(3) and provides substantial private benefit to persons who do not belong to a charitable class.

Charitable purposes include relief of the poor and distressed. See Treas. Reg. § 1.501(c)(3)-1(d)(2) of the regulations. ORG's down payment assistance program does not operate in a manner that establishes that its primary purpose is to address the needs of low-income people by enabling low-income individuals and families to obtain decent, safe housing. The down payment assistance program did not serve exclusively low income persons.

Despite the representations in its correspondence concerning its application for exemption and amended articles of incorporation, ORG did not have any income limitations for participation in its DPA program. It did not screen applicants for down payment assistance based on income. ORG records do not include any data on the buyers' incomes. Instead, the program was open to anyone, without any income limitations, who otherwise qualified for these loans.

The President of ORG stated that the organization relied upon the lenders to do their due diligence in determining that the buyers meet FHA guidelines for loans. In addition, the ORG DPA program does not limit assistance to specific geographic areas or target those areas experiencing deterioration or neighborhood tensions. ORG made down payment assistance available for buyers of homes throughout STATE and in other

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states including STATE, STATE, and STATE. See Rev. Rul. 70-585, Situation 4. The down payment assistance was available for any property that is otherwise is able to qualify for a mortgage as long as the seller was willing to agree to pay the "gift/grant" amount and the fee. Arranging or facilitating the purchase of homes in a broadly defined geographic area does not combat community deterioration or serve other social welfare objectives within the meaning of section 501(c)(3) .

Only an insubstantial portion of the activity of an exempt organization may further a nonexempt purpose. As the Supreme Court held in Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279, 283 (1945), the presence of a single nonexempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

Even if ORG DPA program were directed to exclusively low income individuals or disadvantaged communities, the organization's total reliance for financing its DPA activities on home sellers or other real-estate related businesses that stood to benefit from the transactions, demonstrates the DPA program is operated for the substantial purpose of benefiting private parties.

Like the organization considered in American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), ORG is structured and operated to assist the private parties who fund it and give it business. Sellers who participate in this DPA program benefit from achieving access to a wider pool of buyers, thereby decreasing their risk and the length of time the home is on the market. They also benefit by being able to sell their homes at the full listed prices or by being able to reduce the amounts of the negotiated discounts on their homes. Buyers who participate in the DPA program benefit by being able to purchase a home without having to commit more of their own funds. Real estate professionals and builders who participate in the ORG DPA program benefit by selling more homes due to lowering seller fees, selling homes faster with a qualified pool of buyers, making more money with selling homes at appraised/listed prices; and receiving of funds more quickly through the ORG process of wiring funds within 24 hours. The ORG DPA program provides private benefit to the various parties in each home sale.

The manner in which ORG operated its DPA program shows that private benefit to the various participants in the program was the intended outcome of ORG operations rather than a mere incident of such operations. ORG's down payment assistance procedures were designed to channel funds in a circular manner from the sellers to the buyers and back to the sellers.

To finance its down payment assistance activities, ORG relied exclusively on sellers and other real estate related businesses that stood to benefit from the transactions.

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ORG neither solicited nor received funds from other sources except for about 1% of its revenue in 20XX.

Before providing down payment assistance, ORG took into account whether there was a home seller willing to make a contribution to cover the down payment assistance the applicant had requested. The organization required the home seller to reimburse it, dollar-for-dollar, for the amount of funds expended to provide down payment assistance on the seller's home, plus an administrative fee of several hundred dollars per home sale. In fact, ORG secured an agreement from the seller stipulating to this arrangement prior to the closing. No DPA assistance transactions took place unless the organization was assured the amount of the down payment plus the fee was paid by the seller upon closing.

ORG receipt of a home seller payment equal to the amount of the down payment assistance in virtually every transaction indicates that the benefit to the home seller (and others involved in the transaction) is not a mere accident but rather an intended outcome of the organization's operations. In this respect, ORG is similar to the organization considered in Easter House which provided health care to indigent pregnant women, but only when a family willing to adopt a woman's child sponsored the care financially.

Based on the foregoing, ORG has not operated exclusively for exempt purposes, and, accordingly, is not entitled to exemption as an organization described in section 501(c)(3).

The government proposes revoking the tax exemption for ORG effective January 1, 20XX. The organization operated in a manner materially different from its representation its application materials in that it did not restrict its down payment assistance to low income individuals. Revocation of a determination letter may be retroactive if the organization operated in a manner materially different from that which was originally represented. Treas. Reg. § 601.201(n)(6)(i), § 14.01; Rev. Proc. 2003-4, § 14.01. ORG's operation of its DPA program in a manner materially different from the description provided in its application materials for exemption justifies retroactive revocation of its tax exempt status.

TAXPAYER'S POSITION

The position of ORG is that it has tried to remain true to its mission in helping families achieve homeownership and that it has have run its non-profit organization with the utmost integrity. ORG is proud of the fact that over 90% of the money it has received

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has been given to low-to-moderate income families purchasing homes. ORG states that it has have been dedicated to educating home buyers to be more responsible homeowners in the community. ORG maintains that it has provided education through its ongoing first time homebuyers, default management, loss mitigation and foreclosure prevention courses. In addition, ORG states that it has provided loss mitigation services and kept homebuyers from going into default and foreclosure. ORG states that, since inception, it has been able to keep homeowners in their homes by making their mortgage payments without a charge or a repayment for this service. As of October 20XX, ORG maintains that it no longer provided seller assisted down payment assistance. .

CONCLUSION

In order to qualify for exemption under section 501(c)(3), an organization must be both organized and operated to achieve a purpose that is described in that code section. The ORG DPA program did not operate exclusively for an exempt purpose as described in section 501(c)(3). ORG provided down payment assistance to individuals and families for the purchases of homes regardless of their income levels or needs. ORG DPA activities did not target neighborhoods in need of rehabilitation or other relief, such as lessening neighborhood tensions or eliminating prejudice and discrimination.

ORG operated in a manner indistinguishable from a commercial enterprise. The organization's primary activity was brokering transactions to facilitate the selling of homes. ORG brokering services were marketed to homebuyers, sellers, realtors, lenders, home builders, and title companies regardless of the buyers' income levels or needs and regardless of the condition of the community in which the home is located. Alliances were built with the realtors, lenders, home builders, and title companies to assure future business for the mutual benefit of the participants. Although ORG may have engaged in some educational and charitable activities in its homebuyer education programs and payment of some mortgage payments, its primary activity was facilitating down payment assistance to any individual who qualified for a loan without regard to income provided that the seller had agreed to pay the down payment assistance amount to ORG. ORG is not operated exclusively for exempt purposes within the meaning of section 501(c)(3).

For the foregoing reasons, revocation of exempt status is proposed. Because the facts show that, in 20XX, ORG Foundation, Inc. operated in a manner materially different from that represented in its application for exemption (Form 1023) and related supporting materials, the government proposes the revocation be effective January 1, 20XX.